Mr. R. V. LeSueur.





# The Province of Alberta

IN THE MATTER OF "THE NATURAL GAS UTILITIES ACT"

—and—

IN THE MATTER OF an Enquiry into Scheme to be adopted for Gathering, Processing and Transmission of Natural Gas in Turner Valley

G. M. BLACKSTOCK, Esq., K.C., *Chairman*

Dr. E. H. BOOMER, F.C.I.C., *Commissioner*

*Session:*

CALGARY, Alberta June 20th, 1945.

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# I N D E X

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WITNESSES



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CROSS-EXAMINED BY MR. BLANCHARD:

Q Mr. Kirkpatrick, in your M 9-44 you have your summary of total estimate of cost including depreciation, return on capital employed and administration and the return is based on return to you of 15.56 percent ?

A In the actual for 1944, sir ?

Q Yes.

A No, not the actual. I am speaking of M-9.

Q For the estimated 1944 ?

A Yes, that is 15.8333 gross.

Q Then when you come to your actual 1944 which is set out as part of Exhibit 78, you give us your returns, your rate of return as 7.046 percent ?

A Yes sir.

Q Instead of the 9½ percent ?

A Yes sir.

Q As estimated on the basis of M-9-A ?

A Yes sir.

Q Now then in your Exhibit 78, in your summary of the total actual cost, in calculating your 7.046 rate of return going value, you have included in your rate $200,000.00 for going value ?

A Yes sir.

Q That was not included in your rate base in your M-9-A ?

A No sir that is correct.

Q Now why was that ?

A Well this going value was not included in Mr. Hill's Exhibit 59 at the time we commenced the preparation of that. That was

a subsequent insertion, the going value. I have forgotten the exact date, but it was definitely subsequent to the date we commenced preparation of these estimated schedules.

Q Do you know why it was not included in the first place in Mr. Hill's appraisal ?

A Why the going value was not first included ?

Q Yes.

A No sir I do not know why he did not include the going value.

Q I wondered if it had been discussed ?

A Not with me.

Q So that the addition of the $200,000.00 in your rate base in calculating the rate of return actually for 1944, that has reduced your rate of return by adding that ?

A Oh yes.

Q Now going again to Exhibit 78, the return on your capital was $346,838.20 ?

A Yes sir.

Q That is correct ?

A That is correct, sir.

Q Now then if the tax were 40 percent, on 40 percent basis, that is your income tax, then the income tax would have been $138,735.00 ?

A Well I have not checked it. That is approximately correct.

Q Approximately correct ?

A Yes sir.

MR. CHAMBERS: What was the figure ?

MR. BLANCHARD: $138,735.00.

Q Instead of which you actually paid for income tax $163,191.69 ?

A That is right sir. Not paid, but we have computed that as being the amount which will eventually be paid.

Q That is your assessment ?

A No sir, not our assessment. That is our computation of what the assessment will eventually be.

Q And on what basis did you compute that since it is not computed on a 40 percent basis ?

A The computation is arrived at by taking the $346,838.20, being the profit for the year 1944 before taxes and eliminating therefrom the depreciation which would be disallowed by the Income Tax Department on those assets already depreciated by Royalite Oil Company to that extent and subsequently acquired by Madison with one or two other incidental inadmissable items such as incorporation expense, some $1500.00. I am quoting these figures from memory, but that is substantially the amount of the latter deletion.

Q You use the word eliminate depreciation would not be allowed. You mean added back ?

A Yes I am saying it the other way. I mean added back, disallowed depreciation is added back which has the effect of creating higher taxable profits before tax.

Q If Madison had purchased the full gas system from a stranger then I take it your depreciation could have been based, or would have been based on the cost paid by Madison to the stranger for the purchase of the system ?

A I have every reason to believe that.

Q But since the purchase was made from an affiliate, you cannot capitalize the gain, the capital gain. At least you cannot use

the capital gain as the basis for the depreciation ?

A No sir, inasmuch as it fails to qualify as a transaction between strangers. The Tax Department will only permit depreciation for tax purposes to be continued on the original cost and not on any other cost which would be set up on the Company's books.

Q Then it would be fair to say, would it, that the depreciation that is taken into account by the Income Tax Department is based on the historical cost in this instance ?

A That is correct, yes.

Q Because you purchased the system from an affiliate ?

A Because we purchased the system from an affiliate and the management control is substantially the same.

Q Now then the fact is that Royalite had already written off for some assets ?

A Some of the assets acquired by Madison.

Q Yes, in the books of Royalite.

A I cannot confirm that from memory but I believe that you have a correct statement.

Q And has heavily depreciated many of the others ?

A Yes.

Q Quite properly ?

A Yes, that is correct.

Q So that the result is really that Madison cannot now get the full measure of depreciation ?

A No sir.

Q Now then there is another thing Mr. Hill has taken as part of his value on appraisal, 9 percent general overhead cost. That

is in appraising the value of the Madison assets. Now would that be recognized or will that be recognized by the Income Tax Department as capital subject to depreciation ?

A Oh no, they will take no recognition of any difference between the original book cost on Royalite and whatever figure Mr. Hill may arrive at, whether it is 9 percent or any other figure.

Q As a matter of fact these overhead costs were never capitalized on the books of Royalite ?

A Were never capitalized on the books of Royalite.

Q They were charged in the books as an expense and so represented from year to year ?

A Substantially so. There are some minor items which were capitalized but they are insignificant to the total proportion of 9 percent which Mr. Hill has.

Q Well then Royalite - three things happened I think that affect now the depreciation that Madison is entitled to receive from the Income Tax Department. First, Royalite charged as expense from year to year items that might have been capitalized. Such for instance as general overhead ?

A Items which might have been capitalized, yes sir, but which were just as properly accepted by the Tax Department in those years as expense. They were satisfied there was just as much propriety in expensing those as in capitalizing them. I do not think they expressed any definite opinion one way or the other.

Q But now Madison cannot depreciate any of that capitalized cost ?

A No sir, because it has been in five years.

Q And consequently Royalite took a high rate of depreciation on capital ?

A They took a higher rate than is now being suggested by Madison. I would not like to say it was a high rate in light of the circumstances at that time.

Q And the third thing is, that by reason of the fact that Madison bought from an affiliate and not from a stranger the basis of depreciation can only be on the historical costs on the books of Royalite ?

A That is correct.

( Go to Page 2130 )

Q In your M-9-A/44 and the same is true of 45, 46, 47 and 48, your return on capital employed in that submission is on the basis of 15.833% is it?

A Yes sir.

Q What I want to be clear on is this that Madison is not asking for a 9½% return on this capital plus whatever taxes it was to pay?

A We are asking for a 9½% but in the compilation of the M-9 statements it is necessary to express that in terms of the greater sum or gross figure. Now we did not at the time when we were preparing M-9 know what the incident of taxes effectively would be and we used the 40% rate. My view is that any income taxes are acknowledged or rather are viewed as an expense determining a service rate for utility companies. We have used a 40% rate in arriving at that 15.833% but it might be a 30% rate eventually, or 25 or something like that.

Q Yes, I know, but what I amgetting at is this, in view of the fact that you are not permitted by the Income Tad Department depreciation on the basis of your submission M-9-A, do you now say that you want a clear 9½% return on your capital?

A Yes sir, that is what our statements are intended to arrive at.

Q Plus whatever income tax may have to be paid?

A Yessir, that is right.

Q And if that income tax is more than 40% by reason of the fact of the taking of heavy depreciation by Royalite by reason of Madison having purchased from an affiliate and not from a stranger, the consumers will have to pay more taxes.

A They will if that is the accepted principle. They will certainly pay more than the 40% rate and be booking the taxes as paid.

Q In your 1944, in the year 1944 you estimate they will pay some, what?

A $163,000.00.

Q And how much difference more than the 40%, $25,000.00 more than the 40%?

A That is the spproximate difference, yes.

Q And your submission is that that is a proper way or a proper basis for your rate of return?

A Well my submission is that since taxes and income taxes are treated as operating expenses, any future service rate we have must perforce have the taxes as paid whatever that might be.

Q All right.

Q THE CHAIRMAN: Without reference whatever to depreciation that may be payable or deductible on a public utility basis of the income tax which you pay, if Royalite had continued this as a separate branch?

A I think so, sir.

Q MR. BLANCHARD: All right, then let us go on to our Exhibit 78 again. You have on the last page of Exhibit 78, you have it that your profit for the year 1944 before taxes was $346,838.20?

A Yes sir.

Q And you estimate at least on the basis of your M-9-A-44 in order to get your return of 9½%, you required $383,840.06?

A You are now referring, sir, to M-9-A estimated, are you?

Q Yes?

A Well.....

Q Well there is a deficit of, or at least let us say you are budgetting in your M-9-A/44 for $383,840.06, and you realized only $346,838.20?

A That is right.

Q So that there was a deficit of $37,000.00 in round figures?

A That is right.

Q Now I notice that in your external charges as shown on your summary of actualcosts in Exhibit 78, charges to Royalite, that is charges to the Royalite absorption plant that is supposed to be, is it?

A That is right, sir.

Q Amounted to $30,630.00, is that right?

A Yes, that is the correct figure, thirty thousand, six hundred odd dollars was charged.

Q Was charged?

A Yes sir.

Q Now you have in your exhibit M-9-A-44, and in your submission you fixed your estimate of $56,084.08 as being the amount which would properly be paid by Royalite for those services?

A Yes sir.

Q So that there you have a difference or a deficit of $25,254.00?

A That is correct, and that requires some explanation. I might have done that yesterday. M-9-A-44 estimated was based upon the charge to the Royalite gasoline plant for its absorption operations for the wet gas extracted and its equivalent plant fuel in accordance with the computations set forth in M-12, which is very complicated, but it amounts to a suggested 3 cents per thousand cubic feet, and on that basis we said at that time when the estimated 1944 was prepared that charge would amount or should amount to $56,000.00.

Q Yes?

A Now.....

Q I beg your pardon?

A Now at the time we were requested to prepare, requested by Mr. Fenerty to prepare the contents of Exhibit 78, we prepared

this actual 1944 which includes the actual charge to Royalite, which is $30,000.00, which we submit is too low, but as I mentioned earlier in the Hearing some weeks ago, this was merely, it happens to be a 5% rate, and it has no relationship to fact. It was merely picked out as a starting point, as a tentative rate. We understood when we finally got down to the point where we had what we thought was a proper charge, that it might be more, and it is, sir. That thirty thousand is the actually charged amount, but if the 3 cents per thousand had been utilized, or used in 1944, that thirty thousand figure would be the highest sum.

Q In other words, if you had applied the basis which you have set out in your M-12, that is as the basis upin which Royalite should contribute to transmission costs, you would have charged $56,084.00?

A Yes sir.

Q And not the actual charge of $30,000.00?

A Yes, that is correct, sir. We certainly would. It happens that our computations in the estimated period 1944, were made late in the year, and this $30,000.00 was merely made on a tentative basis.

Q Your actual charges to Royalite in 1944 were based on the very first submissions that you made?

A That is right.

Q That was that Madison would receive 25% of the sales from absorption gasoline, distribute 20% to the producers and retain 5% for its services?

A That is correct. And we did not suggest that 5% was right or wrong. That was in the interim.

Q It was on that basis that you charged Royalite for 1944?

A Yes, it was a charge that was subject to change.

Q And you did not consider that a charge on a proper basis?

A No, I consider it is too low.

Q So that Royalite should pay now to Madison $25,284.00 for 1944?

MR. CHAMBERS: That does not necessarily follow. I want to make my position clear. We are talking of the 1944 operations, and the charges as between these two companies are not of very much importance one way or the other, I submit, because the Board's regulations, as I understand it, are going to be from the 1st of January, 1945. I mean that if Royalite has been charged too much or too little it comes out in the wash on the 1944 operations because they must stand on what they got.

MR. BLANCHARD: Yes.

THE CHAIRMAN: I think your questions are a perfectly proper deduction in putting them to the witness as something which must necessarily follow from the evidence given.

MR. BLANCHARD: What my learned friend has suggested is this, instead of my asking questions the Board should consider that. That is quite satisfactory to me.

THE CHAIRMAN: Yes.

Q MR.BLANCHARd: Is the purpose of Madison to capitalize this deficit for 1944 on the opening rate base of 1945?

A No sir.

Q It is not?

A No.

Q Who is going to take the loss?

A I think it could be done in one or two days. If this Board views with some agreement our suggested 3 cent per thousand cubic feet, then I think that an adjustment relative to the year 1944 could thereupon be made and booked in 1945, in connection with the Madison Company. On the other hand, if

it is felt that there is no necessity for adjustment between the companies relative to 1944, this deficiency then, of course, will have to be ignored but it would not in any event be suggested by Madison to be capitalized as part of the rate base.

Q Now I notice, too, in your summary of actual costs for 1944, Exhibit 78, that there is a deficit of $3549.00 in the Boiler Plant operations?

A Yes sir.

Q Now I think it has been established by you that Royalite and the Valley Pipe Line utilized 75% of the steam?

A It is on the order of 75%, yes sir.

Q So that Royalite and the Valley Pipe Line could absorb 75% of that loss in the Boiler Plant?

A Yes sir, and they will absorb that loss.

Q And they will absorb that loss?

A Yes, but not by way of adjustment in the same calendar year. I just want to make perhaps a little explanation of that. I mentioned yesterday that throughout the year it is necessary to compute the cost to make a thousand pounds of steam, or the cost to make a kilowatt hour of electrical energy, and throughout the year those costs are charged both to Madison's own internal operations and to its external customer. Naturally it would not be possible to us to make that work out to the last red cent. It would take time to do that.

Q That is adjusted later?

A It is adjusted by giving effect to this deficiency in computing the estimate for the fall of the year.

Q I see. I am just trying to find out where there is a deficit of $30,000.00, where it lies, that is all, and then I think you have a deficit in direct operating costs in excess of your $30,000.00, $20,000.00 for contingencies to the extent of

$3,012.00?

A I do not follow that question.

Q I say that you have a deficit on direct operating costs over and above the $20,000.00 budgetted for contingencies amounting to $3,012.00.

(Go to Page 2137)

In other words, your operating costs absorbs the twenty thousand dollars?

A Yes, sir.

Q And in addition you had three thousand and twelve dollars of a deficit?

A Well I am not certain where the three thousand and twelve dollars comes from, Mr. Blanchard.

Q By the way, why did you take that 9½ per cent rate of return? How did you arrive at that?

A That is the rate that I was instructed to use in making up this costs statement for the five-year period.

Q Do you know who suggested that rate?

A Mr. Trammell instructed me to use that rate.

Q When this transfer of assets was made from Royalite to Madison, did you consider issuing bonds instead of non-par value stock to Royalite?

A I gave no consideration to that?

Q Was it discussed do you know?

A Not in my presence, no sir.

Q If you had issued bonds for the purchase price of the gas system instead of stock it would have resulted in very much lower income tax so far as the Madison Company is concerned.

A Treating bond interest as an expense of the Company.

Q Yes.

A Yes, sir, that is right.

Q That could have been done?

A It would have transferred the incidence of income tax to the shareholder Company.

Q Why was not that done, do you know?

A I do not know, sir.

Q It would really have meant that the Royalite would have been assessed for the income tax that is now paid by the consumers or will be.

A That would have been the effect of it, as I understand it.

Q Now then, you have in your Exhibit 78 under your Gross Operating Cost in your summary, a sum of $1199.90 for repressuring system, that is depreciation expense and return on capital.

THE CHAIRMAN: Where does that appear?

MR. BLANCHARD: In the Summary in Exhibit 78.

A Yes sir, I see it.

Q Do you not think that item should be deferred till 1945?

A I mentioned that yesterday. If it is decided to defer that charge I would not disagree with that.

Q It is not ascertained yet who has to pay that?

A No sir.

Q So there would be no objection on your part if that was deferred?

A I do not think so, no.

Q Now then, if you look at M-D-9, 44 page 1.

A Which schedule is that?

DR. BOOMER: M-9-D.

Q MR. BLANCHARD: In M-9-D 44, page 1, you have Capital Additions. This is in column 2. Number 1 Main Compressor Plant, $63,000 for the half year.

A Yes, sir.

Q Does that mean an expenditure of $126,000 for the year? That capital expense is all due to repressuring equipment, is it now?

A No, I do not think that is so, sir.

Q Can you tell me how much of it is?

A I will just have to take a moment to see if I can trace that figure for you. I am afraid I cannot tell you the exact composition of that figure at the moment without referring to my working papers.

Q I may be wrong in saying that that whole Capital Expenditure is for re-pressuring.

A It is substantially a compressor proper and some other equipment.

MR. McDONALD: That is shown in M-7 and 8, is it not?

A It does not distribute it, Mr. McDonald, to the plants as shown on this schedule.

Q MR. BLANCHARD: Let us assume that it is for the moment, just for the sake of argument, let us assume that it is all for repressuring. That Capital Expenditure I have mentioned is for repressuring, let us assume that. Now then, if that is so should not the depreciation and the return on that capital expended for repressuring also be deferred to 1945?

A If it were all exclusively installed for the purpose of repressuring, I think I would agree to that suggestion.

Q Then it would be proper for you at some time to break that down and let us know how much is for repressuring equipment?

A I will be very glad to try during the recess, if you wish.

Q I do not know whether it can be done readily or not. Now M-14, page 2. You mention that the distribution of the total cost of the Number 3 South Compressor Station was made on the estimated horsepower requirement basis. I

think the same expression is used when you refer to repressuring.

A Yes.

Q To try to fix the repressuring costs?

A Yes, sir.

Q Now will you just explain to the Board, for the record, what you mean by estimated horsepower requirement basis and why you adopt that basis?

A The estimating of the horsepower requirement basis was actually computed, of course, by the field operating people who are familiar with the method of determining that so I am not able to tell you how that is computed. But we suggested it from the accounting standpoint as probably a fair and proper way of distributing the total cost of operating these stations as a whole, admitting that there would be certain direct items such as lubricating oil or engine repairs related to the operation which could be specifically identified. As I mentioned yesterday, and I believe it is set forth in this submission M-14, we used the horsepower basis throughout the years 1944 and 1945 to illustrate the incidence of cost.

Q Apparently you consider that a fairer basis than the volumetric basis.

A I think it is fair, sir, because the volumetric basis would not necessarily bear a proper proportion, in our opinion, of the total direction, operation, repairs and maintenance at these stations. We think the horsepower basis is the proper way to do it.

Q Generally speaking, it would take more horsepower to repressure a thousand cubic feet of gas.

A That is right.

Q. Than to put it through the transmission lines?

A More effort is required to put gas in the ground than is required to pump wet gas in the first instance.

Q That is probably why you adopted the horsepower basis, was it, rather than the volumetric method?

A We think it is a measure of effort and wear and tear that is occasioned.

Q THE CHAIRMAN: If I were an independent operator, Mr. Kirkpatrick, using horsepower, would you give me the electricity, steam and water on that basis?

A No, sir, on the basis of the service which you actually consumed. That is to say the proportion of steam and electricity. I think in that case we have something tangible which can be measured.

Q I am speaking now of an independent business. I am an operator and I go into the Turner Valley field and I come to you people and I say "will you give me steam and water and electricity?" and I want to know on what basis you would give them to me to run my business.

A I think it would be on the basis of, on the same basis that we sell power and steam to the Valley Pipeline Company and to Royalite. If the total cost of operating the plant is so much money and the proportion of the service which you require is ten per cent, then I think it would be proper to suggest ten per cent of the total cost would be the amount to be paid.

Q DR. BOOMER: And no profit?

A Well our costs throughout, Sir, include depreciation and the suggested rate of return. The profit is apparent in the cost.

Q THE CHAIRMAN: If you did not distribute any part of that working capital in reaching that cost. . . . .

A Yes, we do.

Q I thought you said you did not allocate any of the working capital to those plants.

A No sir, I said we did not distribute the working capital to such services as the head office, field office, transportation but the two main service plants, the boiler plant and the electric plant and all other functioning plants, they bear their proportion of the working capital both cash and material and supplies.

(Go to page 2143)

Q MR. CHAMBERS: That is shown in an exhibit, is it not?

A Yes, it is set forth in an exhibit.

Q MR. BLANCHARD: Now in your M-14, I think you mentioned an item of a charge made to the British American for transporting gas, that would be between....

A The Hartell Junction.

Q The Hartell Junction and the No.I Plant?

A The Scrubbing Plant.

Q The Scrubbing Plant, yes, and that is fixed on the basis of a thousand dollars a month?

A Yes.

Q That is not an agreed sum?

A It is a sum set forth in the Board's order of January 5th, 1945. It is not an agreement between Madison and British American, no. The Board had set that .

Q There is no agreement at so much per thousand cubic foot?

A No, there is no agreement between the Madison and the British American. The Board has set by order that it should be 6/10 of a cent or one thousand dollars a month, which ever shall be the greater.

Q I suppose unless this whole system goes bankrupt, it does not really much matter so far as the consumer is concerned, whether that is fixed at a lump sum or at so much a thousand cubic feet, it is either paid by you or paid by the British American Company, I mean if it should be $1,500.00 a month instead of a thousand and the British American only gets a thousand, then the British American will receive the difference in the cost of delivering gas?

A Yes. If the real cost to them is in excess of a thousand dollars.

Q But you used this to make up your submission?

A That is so.

Q Now going to M-13, Mr. Kirkpatrick, on your schedule which is a summary of estimated scrubbing costs to determine the costs per m.c.f. of total gas scrubbed and the cost per m.c.f. of total scrubbed gas sales, you arrive at an average figure in your column 7 of 2.19 and a fraction cent per thousand cubic feet for gas scrubbed?

A Yes.

Q And 2.37¢ for total scrubbed gas sales?

A Yes.

Q Which figure do you wish us to take?

A Well our reason for joining those two bases in there in item "A" we thought it wise to show what the actual cost was of scrubbed gas regardless of its ultimate destination in the event that this Board might wish to consider that question.

Q That is which is scrubbed?

A Yes.

Q MR. CHAMBERS: Does that include Bow Island?

A All scrubbed gas estimated to be scrubbed anywhere is included in that column under item "A".

In "B" we have shown the equivelant cost per m.c.f. in terms of the scrubbed gas which is sold and which at the present time is the only source of scrubbing income.

Q Well then the difference between the two figures represents gas which was scrubbed and not paid for?

A That is right.

Q And that includes the gas from the Bow Island?

A Yes.

Q Which does not amount to much, I think it is forty million

cubic feet a year?

A Something in that order.

Q Now nobody pays for that?

A No Sir.

Q What?

A No Sir, that is correct.

Q For whose benefit does Madison gather, transmit and scrub that gas if nobody pays for it?

A Well I think, actually in my mind they are scrubbing that gas for the benefit of an agreement between Royalite and The Canadian Western Company.

Q Yes, all right. What about the scrubbed gas which is stored in Bow Island, that of course is not paid for?

A It is not. The cost of scrubbing is not being paid to Madison at the moment, no Sir. The gas itself is being paid for by Royalite under the Board's order of recent date.

Q Yes?

A And that was I think, if I recall the wording, it says that that price is exclusive of gathering, compressing and other costs.

Q Well I have not got the exhibit before me but the agreement between Royalite and the Gas Company is in as an exhibit?

A Yes, that has been submitted.

Q I do not think you need to go into it unless you want to. I think the agreement provides that Royalite is to gather and compress and scrub the gas and put it into the lines of the Gas Company for storage in Bow Island and then is to receive so much per thousand cubic foot for it?

A At the time of its withdrawal.

Q At the time that it is used?

A Yes.

Q And no time was fixed in the agreement as to when it would be used?

A No.

Q So that that scrubbing, ... we are dealing only with scrubbing for the moment,- that scrubbing was a function that Royalite had to perform in compliance with the terms of the contract you just mentioned?

A That is right.

Q And it is a function.....

A Prior to January 31st, 1941.

Q And it is a function that now Madison is performing?

A That is correct.

Q For nothing?

A Was that a question you asked me, Sir.

Q For nothing?

A It is not receiving any income for the scrubbing costs of the gas being stored in Bow Island.

Q As a matter of fact there has been no gas stored in Bow Island for sometime?

A There is a little gas being stored at the present moment commencing sometime in May of this year.

Q And I think you anticipate or it has been estimated that there will be about five million cubic feet a day stored in Bow Island during the summer months?

A I think those are the figures which have been given.

MR. CHAMBERS: I do not want to interrupt but while you are following up the Bow Island picture I think for the purposes of the record, one of the questions you asked Mr.Kirkpatrick might have implied an interpretation of that contract. Now

the Royalite position is so far as the Royalite contract with the Gas Company for storing gas in Bow Island is concerned, it is that Royalite only supplies it if it has gas available. That is the position up to the passing of this act , and Royalite has taken the position from then on that it has no gas available and it was not concerned about storing gas in Bow Island. A situation came up this summer whereby there was certain gas that could be flared which did not go to Bow Island and the Board granted an order, a temporary order to take care of that situation, orders Nos.15 and 16. There might be some indication, - I do not know, to anybody reading this transcript, that Royalite was now not living up to its contract and was loading on to Madison something itself was under obligation to do but the point is that this contract so far as Royalite is concerned as to the question of Bow Island, that is the situation and it is prepared to stand or fall on its interpretation of that agreement. If somebody wants gas to Bow Island Royalite says "Well we are prepared to do it on certain terms."

Q MR. BLANCHARD: Royalite is under no obligation to deliver any gas to Bow Island?

A That is it.

Q But it has to be considered at sometime?

A Yes.

Q Now let us go to M-12?

THE CHAIRMAN: You had finished with this, had you Mr. Blanchard, or do you wish to go further with it.

MR. BLANCHARD: I think unless you, Mr. Chairman, want to pursue it further, I have nothing more to add.

Q MR. BLANCHARD: Now M-12. Now for the purposes, of the submission, submission 12 has four main objects, or rather you

had four main objects in preparing M-12, the first is to determine the total cost of gathering and compressing?

A Wet gas gathering.

Q Wet gas gathering and compressing?

A Yes.

Q And the second was to split the cost in the No.I Plant between gathering and compressing?

A That is right.

Q And the third is to split the cost in the No.3 Plant between the gathering and compressing of the residue gas?

A That is right.

Q And the fourth is, and I suppose one of the main purposes, is to determine the percentage of compression and gathering costs payable by Royalite?

A Yes.

Q And on that basis, at least in your submission you fix or you arrive at the figure of, M-12-D, Page I, on page I of 12-D, which is the distribution of wet gas gathering and compression costs, you find that the total percentage which should be paid by the Absorption plant is 9.54?

A That is right.

Q Now 7% of that, the first two items consist of plant vapors and absorption gas extraction?

A Correct.

Q Now in column 5 of 1944,- let us take 1945 rather because there was not the same question in 1944, - the total volume of wet gas, compressed gas, gas compressed at the No.I Plant would be 18 billion 322 million 300 thousand?

A That is our estimate.

Q And 7% of that would be 12 billion, no, or one billion, 282

million, 561 thousand?

A If you take 7% of 18 billion, I assume that would be correct. It sounds all right.

Q Now that leaves the balance of wet gas compressed at the No.I Plant of 17 billion, 39 million odd?

A Yes.

Q Cubic feet?

A Yes.

Q Now I am informed that Madison delivers to the scrubber for scrubbing or did, it will, that is an estimate made I think by your officers, will deliver to the scrubber in 1945, 13 billion, 100 million cubic feet, which leaves 3 billion 939 million cubic feet unaccounted for, I mean there is somewhere around that point. Now what is it, do you know?

(Go to page 2150)

A Well I had to use the figures again to actually reconcile them, but there appears in your explanation to be two items unaccounted for. One is the volume of residue dry gas being returned to the north return fuel system. The other is the metering differences. The two of them would not quite to my mind equal the approximate three million cubic feet you spoke of.

Q Just a moment. Did you say residue dry gas to the north fuel line ?

A Yes sir, that is what I said.

Q Oh yes, that is right. I was thinking of scrubbed gas.

A It is unscrubbed gas.

Q Well I am taking again your estimate. I find that fuel would account for 817 million cubic feet. By the way, I have here, I find the return for returned fuel for 1945 to be 1,095,000,000 cubic feet ?

A That figure sounds familiar to me. I believe it is taken from Mr. Stevens-Guille's M-2 revised.

Q Now that is something that is not taken into account in the fixing of the percentage that should be borne by Royalite ?

A It is not taken into account in that percentage, no sir. That 9.4 percent is the volume relating directly to the extraction of the liquid content of the wet gas leaving the remaining volume representing residue gas in some form or the other, either scrubbed or unscrubbed, eventually for return north to the wells drilling in that year.

MR. CHAMBERS: Pardon me, Mr. Blanchard, for interjecting. I am speaking now on behalf of Royalite. These costs as set up do include in the charges that indirectly go from the Gas Company to the consumer, the cost of bringing down residue dry

gas that ultimately goes back for drilling purposes in the north end and Royalite instructed me to say they realized that should be charged to them and is a factor that will be taken into consideration when the adjustment takes place between the absorption plant and producer as to the percentage.

MR. BLANCHARD: Well I think that is a very fair statement from my friend.

Q In other words the gathering and compressing of all the gas later returned to the north end for fuel, the proportionate costs of that will be borne by Royalite. Now of that nearly four billion cubic feet unaccounted for, that is not paid for anywhere. I find that there is repressured 2,349,000,000 is expected to be repressured in 1945. How is the cost of repressuring taken care of in your statement ?

A The cost of repressuring is set forth in all our Exhibits M-9. It is the last item on the group of costs headed "Operating Department" . I think probably what you have reference to, if I may say so, is the gathering costs of the repressured gas. The gathering cost of that gas which is repressured is not transferred by us in these submissions to the repressure system costs.

Q Then if your submissions were accepted that gathering cost would be charged to the consumer ?

A That is correct, yes.

MR. HARVIE: What was that question ?

MR. BLANCHARD: Then if the Madison submissions are accepted the gathering costs of gas repressured would be charged to the consumer.

Q And again when the gas that is repressured is delivered to the

consumer there will be another gathering cost to be paid by the consumer ?

A It will be a mighty insignificant one, because the repressured wells are in the immediate vicinity of the scrubbing plant. It will not be transported through the same system, to the same existing gathering system.

Q You think there will be a small amount compared to the original gathering cost ?

A I would want to be corrected on this, but probably it will be returned through the same line as it is now being repressured.

Q If you base your depreciation on the scrubbing sales, then that does not take care of any of these gathering costs where the gas does not go to the scrubber ?

A It imposes as a depreciation. That volume will result in depreciation calculation applicable to the gathering system. Yes sir there will be depreciation.

Q The gathering system handles a very great deal more gas than the scrubbing substantially ?

A Yes, it does handle a substantially greater volume to the scrubber but not necessarily a substantial percentage greater in terms of wet gas reserves. We must bear in mind, if we say twenty million wet gas are transported in and only fifteen million are scrubbed the two must have different denominators in determining the factors to be applied to arrive at the depreciation.

Q In your Method "A" in M-10, you say that the basis should be on the gathering of the amount, the volume of gas gathering costs. It would be necessary to know the gas reserves in some five or six different parts of the field served by different lines ?

A That is one of the objections I raised to Method "A".

Q Do you think it would be necessary to do that ?

A Yes sir.

Q Couldn't you take all the total volume going through the gathering line and use that as a basis ?

A You could do that but in my opinion that is no different than taking the scrubbed gas. You should arrive at approximately the same percentage in that case.

Q You would have a higher depreciation ?

A Not necessarily, no sir. Not necessarily. There is so much wet gas there which is a greater volume than its residue equivalent. If a certain volume of wet gas is extracted during the year that represents the percentage of total wet gas reserves. Let us say it is 5 percent which represents both the wet gas and the wet gas transported and the wet gas reserve, the residue gas base, you will still result in a 5 percent -

Q I have not figured it up but it appears to me if you were handling four billion cubic feet more a year in the gathering system than you are in the scrubbing, if you take your gathering system as a basis you would have a greater depreciation say this year or next year.

A I doubt it sir.

MR. CHAMBERS: If you have your enumerator and denominator both larger, it would not make any difference.

Q MR. BLANCHARD: Now there are some parts of the system in any event that will be written off or at least will cease to function in the course of the next ten years. For instance the G. & O.P. Lines to the compressor and back to the main north line. That is assumed will cease to be used ?

A It is not our assumption sir. We are assuming that the equipment which is related to the gathering of residue gas from G. & O. P. Plant has a substantial alternative use at the end of ten years.

Q Where ?

A In the existing field gathering system. That is an assumption which I think would have to be substantiated by engineering evidence, but it is an assumption we use in our accounting.

Q If the assumption is not correct, do you think that the lines, I suppose there are two of them, should be depreciated within their life ?

A If they have no alternative use, most certainly, yes sir.

Q All right, now what about the repressure installations?

A Well again we have assumed there will be some alternative use for that equipment.

Q I understand that in the submissions it is estimated there will be no more repressuring after twelve years, is it perhaps less ?

A At least twelve, if not more.

Q If there is no alternative use for those installations and equipment and so on that make up the repressuring there is no alternative use for them you would say they should be written off, depreciated during their life ?

A Again I agree when there is no alternative use.

Q And that will result in a higher rate of depreciation in the next few years ?

A In the early years yes.

Q At which time you have got a great many more customers to absorb that depreciation. You are selling 15 billion cubic

feet now and you anticipate in five years you will be selling only 9 billion cubic feet. I was wondering whether your risk is not increased when you defer this depreciation or at least spread it over the whole term rather than take a high depreciation now. It makes a difference in your risk.

A Well I do not think so. Apart from the question of alternative use just assume I take it that this equipment that is used for repressuring and their residue line and compressor from G. & O. P. Plant, assuming they have an alternative use, then I believe that the incidence of depreciation to each m.c.f. of gas disposed of is definitely geared in such a way that if 15 million c.f. are put through this year as opposed to 9 million in four or five years hence the incidence of depreciation is exactly the same.

Q You are assuming there is no greater risk becuase you assume there will be a market right to the end for available gas ?

A I am assuming sir we will withdraw the 360 odd million cubic feet that has been referred to. That it will be all marketable shall we say.

Q There is just one matter I would like to get on the record. Going back to M-9-A. Take 1944. It is just for the record in anticipation of other evidence that will be given Mr. Kirkpatrick. Taking your boiler plant and electric plant. That is the service department charges. Now those are siphoned up into the various operating departments ?

A To the extent that those services are used by those functional operating departments.

Q Now then when a proportion of the boiler plant and electric

plant are siphoned into the direct expense of the, let us say, scrubbing plant, you include the depreciation and the return in the figure that is given as direct expense for the scrubbing ?

A. That is correct Mr. Blanchard.

( Go to Page 2157)-

Q That is correct?

A Yes.

Q And then the depreciation expense in Cooumn 4 on thereturn on capital?

A I will just check that.

Q That is 4 and 5?

A Yes.

Q They are calculated, they do not include, there is no duplication?

A No sir.

Q Of the depreciation rate of return already included in the services?

A No sir.

THE CHAIRMAN: Mr. Fenerty?

.....

CROSS-EXAMINATION BY MR. FENERTY

Q Mr. Kirkpatrick, I believe you have been in Calgary in connection with the Royalite and subsequently the Madison approximately some four or five or six years?

A Five and a half years, Mr. Fenerty.

Q And prior to that you were associated with other oil companies producing or refining gas?

A I was associated with the International Petroleum Company prior to my coming to Calgary here.

Q For some time?

A Some twelve years, fourteen years.

Q And are you familiar as a result of those associations with the general principle employed by petroleum companies, oil companies, in apportioning costs as between departments where there are costs which might be apportioned between different

departments?

A Yes sir.

Q That is common costs?

A Yes sir.

Q And is it correct to say that the general basis of apportionment adopted in the oil industry is based on returns rather than volume?

A By returns you mean realization?

Q Gross returns, realization?

A Not in my experience, sir.

Q It has not been?

A No sir, because my experience has been confined to operations which are wholly integrated prior to my coming to Calgary here, and in that particular operation a substantial part of the affair was producing, with refining as an incidental part, but each of those departments maintained their own administrative groups and the expenses of those groups were a burden directly upon the producing or refining as the case might be. There was very very little expense in the operation which I have reference to, which required an arbitrary distribution between producing, refining, marketing, etc. Each one had its own management and administrative group.

Q Yes.

A As distinct from the operations to which you are referring in Turner Valley, where there is a common administrative group.

Q Then you did not have that same problem?

A No, not to that extent.

Q Now I note in Exhibit 80, Report M-10, page 11, paragraph 19, there is the statement.....

MR. CHAMBERS: Page 11?

Q MR. FENERTY: Page 11, paragraph 19 , dealing with

Method "B".

A Pardon just a minute.

Q And you explain it on the principle that all of Madison's fixed capital assets are dedicated to the fundamental work of gathering and scrubbing and preparing for market residue natural gas for sale to Calgary and other domestic consumers? Now when you are referring to residue gas, preparing the residue gas for the market, I take it that is dry gas, in a word?

A Dry gas to the market, yes.

Q Yes?

A Dry scrubbed gas.

Q So that when you refer to residue gas it is dry gas?

A That is correct.

Q And it follows from that that the assets of Madison are dedicated to the fundamental work of gathering dry gas and scrubbing it and preparing it for the market for Calgary and other consumers, that is right is it not?

A Would you just repeat that question, Mr.Fenerty?

Q I say it follows from your statement that when you refer to residue natural gas as dry gas that the fixed assets, I am quoting now, "Madison's fixed capital assets are dedicated to the fundamental work of gathering and scrubbing and preparing for market dry gas for sale to Calgary and other domestic markets"?

A That is right.

Q I am just substituting the word "dry gas" for "residue natural gas" in the statement as it appears here?

A That is Madison's fundamental work, yes.

Q Now at what stage of these operations does dry gas appear on the scene for the first time?

A Dry gas first appears on the scene at the G.O.P. plant.

Q Yes. As far as the Madison is concerned?

A As far as Madison is concerned it appears on the scene at that point because then it is transmitted to Madison's facilities.

Q Then as far as Madison's own operations are concerned, you distinguish from taking the gas from the G.O.P. or the British American Companies. Take the North end, where does the dry gas first appear on the scene?

A At the outlet at the gasoline plant.

Q Down stream?

A That is right.

Q But you do not start there?

A No sir.

Q And as I understand it the elements which ultimately appear as dry gas first appear on the scene at the bottom of a well, don't they?

A Certainly.

Q And you do not start there?

A No.

Q And how do you come to pick a point in between?

A Well I am not quite certain what the point in your question is. I am afraid I do not understand it.

Q Never mind the point. Just tell me what I asked you. You are not concerned with the point, you are concerned with the facts. How did the company come to pick this place.

A Well in its raw native form it comes out in the well, and the fuel resulting, the residue gas, from Madison's standpoint, is taken over at the outlet to the gasoline plant after the liquefied contents have been extracted therefrom. There was residue gas inherent in the gas from the time it left the well.

Q Let us go over it again, so that we will both get the point.

I think we have it but let us go over it again. You say you are dedicated to the function of handling dry gas but you do not start with dry gas?

A That is correct.

Q That is right?

A Yes.

Q And the product from which you get dry gas starts at the bottom of the well, does it not?

A That is right.

Q That is the first place where you get it from, apart from the gas cap, Mr. Kirkpatrick?

A Yes.

Q I want to know why if this company is dedicated to the function of handling dry gas it does not start to handle dry gas, it starts to handle wet gas, does it not?

A It is wet gas and then it is eventually in the dry gas form.

Q And you have to have oil in your wet gas in the case of the oil wells?

A Yes.

Q Leaving out the gas cap?

A Well the two are produced coterminously, yes.

Q You say you have to handle wet gas in order to have dry gas?

A Yes.

Q And I am going one step further and say you have to handle oil in order to get wet gas.

A We do not heave to handle oil at all.

Q To get wet gas?

A No, we are not concerned with the oil business at all.

Q THE CHAIRMAN: What Mr. Fenerty means somebody has to handle it?

A Yes.

Q MR. FENERTY: Mr. Kirkpatrick, you say you are not concerned with the oil business at all?

A Yes.

Q And you are not concerned with the wet gas business?

A We are dedicated fundamentally for the purpose of preparing and transporting gas to the market.

Q You are telling me that you are dedicated to the function of gathering dry gas, and you tell ke you are not concerned with oil, and you told me, I suggest, in effect, a question or two ago that you are not concerned with the wet gas, is this not logical?

A Well I have not any answer to that, sir. I do not understand what you mean, frankly.

Q The question that I was getting at, and I will ask you to try and give it some thought, why you happened to start your functions somewhere between the beginning of the operations and the production of the thing which you are dedicated to handle, dry gas? Why did you not start at the dry gas end or at the beginning, that is what I want to know?

A You are asking me I take it, then, Mr.Fenerty, why is Madison the owner of the wet gas gathering lines and the dry gas?

Q I am just asking you only what I have said, why you start somewhere in between. Now do you know why?

A I do not understand your question, I am very sorry.

Q You do not understand it?

A No, I do not.

Q You are serious about this, you do not understand what I am saying?

A I do not understand it the way it is put.

Q THE CHAIRMAN: I think it is very simple. Mr. Fenerty is in effect saying to you, why didn't you start at

the outlet to the absorption plant, and since you did not do that, why did you not start at the bottom of the well, and since you did not do that, why did you pick a place in between the two?

A Namely from the top of the well through?

Q That is right?

A That is a question I cannot answer. I do not know.

MR. FENERTY: You do not know?

MR. CHAMBERS: He has not got that answer. I do submit the answer is very simple, and it is not for this witness or any other witness to tell it.

THE CHAIRMAN: Well, Mr. Chambers, if the witness knows.

MR. FENERTY: Just a minute.....

THE CHAIRMAN: He may not know.

MR. CHAMBERS: It is the Legislature that says where the starting point is.

MR. FENERTY: If my learned friend is going to make a statement as to the answer, I am going to give an answer and it has to do with something being a public utility.

MR. CHAMBERS: I do not think the question is proper. I say we start where the Legislature tells us to start in the Natural Gas Utilities Act. It defines it there. That tells us where to start.

MR. FENERTY: He should be able to give us a statement on that. Where you start is something.....

THE CHAIRMAN: Just a minute, gentlemen. This is going to stop. I am not going to have it. Mr. Fenerty's first question was a perfectly proper one and the witness can answer it if he has the information.

Q MR. FENERTY: You say you cannot answer that question?

A No sir, I cannot answer the question in the form that you have put it, Mr. Fenerty.

Q As a result of your experiences in the oil operations, where do you think it should start?

A My experience is not such or has not been such that I could give an opinion as to where it should start.

Q What you have done has been done as an accountant, and you have allocated it on the basis of your instructions, on the basis of the facts that you got?

(Go to page 2165).

Q And were your instructions . . . . . You prepared these reports, I believe, didn't you?

A Yes sir.

Q And were your instructions that the Madison Company was dedicated to handling dry gas?

A That is my observation and I will take sole responsibility for that remark in this report.

Q You must have known something about that, to make that statement.

A I still say their assets are dedicated to the business of handling compressing, scrubbing and so on of dry gas.

Q Yes, I know. But that is the best you can tell me as far as you are concerned then that it is dedicated to handling dry gas and you make that statement on your own responsibility?

A That is right.

Q And you have no knowledge or ideas of why we start with handling wet gas?

A No, sir, I have not.

Q All right, you cannot tell me any more can you. Now I take it in the course of your work you acquire some knowledge of what happens in the field. You would have to know about that.

A A rudimentary knowledge, yes.

Q I take it you do know that gas, as such, in the commercial operation of the field, speaking now of crude oil, the gas first performs the function of assisting in the production of crude oil, the gas lifts up the oil.

A That is right.

Q And that gas is then taken through a separator where the crude oil is separated. Some volume of crude oil and then it

is either flared or taken through a pipe line to the absorption plant, that is correct?

A That is correct, yes.

Q So that leaving out the question of waste, you have first the function of the lifting of the crude oil; second is the production of natural gasoline.

A Yes, the gas is taken . . . . .

Q From there on it has been in the past either flared or used for fuel.

A In certain wells, yes.

Q In all wells, has it not, used either for fuel or flared?

A Yes. There have been a number of wells which have been tied into the system at one time or another, as I understand it. Your statement is correct insofar as some wells are concerned,

Q So we have the natural sequence of events. First, the crude oil operation, the wet gas operation and the residue gas, what you call residue, the dry gas which is sold if there is a market and it is flared if there is not, heretofore. From here on, perhaps, it will either be sold or repressured. I suggest to you in the set-up we have here as advocated by Madison you have reversed that situation that existed heretofore. You are, in effect, treating this operation from beginning to end as a dry gas operation, with a residue of natural gasoline and then back to the well with some crude oil. That is the way you have treated it in your set-up here.

A If I understand your question you are stating that we are taking the dry gas as the end product.

Q Yes.

A And going back through the various stages to the point where it first comes out of the well.

Q Those are incidental by-products. Crude oil and gasoline.

That is your set-up for the purpose of this submission, is it not?

A We are not concerned with anything to do with crude oil or gasoline. We are concerned with natural gas.

Q I appreciate that.

A We are not saying that crude oil is a by-product of the gas or gas is a by-product of the crude oil.

Q My suggestion does not make sense to you?

A I do not understand it, I am sorry. I see what you mean, I think, that one or the other is a by-product of the other.

Q Yes. And I say, for the purposes of this hearing, you have set it up that dry gas is the chief product and the others are by-products, have you not?

A For our purposes, the dry gas is the thing that really we want to get. We want dry gas.

Q And I am right in saying that for the purposes of this Inquiry, you are treating the dry gas as the chief thing and the others are by-products. That is according to your set-up.

A We are in the dry gas business.

Q You do not have to tell me that. I suspected you were in the dry gas business. Anyway, you can tell me if I am right. If you do not know, tell me and if it is not so, tell me.

A I know we are not concerned with crude oil or natural gasoline. Therefore we have no occasion to consider whether they are by-products. I do not see that situation in our set-up.

Q That is the answer as far as you are concerned, it is not so?

A That is right.

Q Then we will leave that.

THE CHAIRMAN: I think we will adjourn, Mr. Fenerty.

(At this point there was a short adjournment.)

Q MR. FENERTY: Mr. Kirkpatrick, just another word about the subject we were on and I will come to something else. I wonder if your understanding is the same as mine that these gathering lines which are owned by Madison, when they are in operation are fully and completely occupied - I mean as to volume - fully and completely occupied with the transmission of wet gas from the well to the absorption plant.

A Yes, they are fully occupied with wet gas.

Q Every bit of that wet gas goes through - and to use a layman's expression - is worked over in the absorption plant.

A With the small exception of any gas that may be used as fuel for heaters, but the substantial part of that gas goes through the absorption plant.

Q I am going to suggest to you, using your own expression here about these things being dedicated to certain uses that insofar as your gathering lines are concerned they are dedicated 100 per cent to supplying wet gas to the absorption plant.

A No, sir, I cannot agree with that thought, that they are dedicated 100 per cent.

Q I was suggesting to you that so far as your gathering lines are concerned, using dedicated in the sense you use it, that they are dedicated 100 per cent to conveying wet gas to the absorption plant.

A No, sir, I do not see that that is right.

Q Do you say they are dedicated 100 per cent to the dry gas industry?

A I do not say that, sir. I say they are dedicated fundament-

ally.

Q Fundamentally?

A Or substantially, put it that way.

Q Now then let us go one step further. Do you say that the separator at the well and the tubing in the well are dedicated fundamentally to the dry gas industry?

A Are you speaking of crude oil wells, Mr. Fenerty?

Q Yes.

A No, sir, they are not.

Q We will get this. The gathering lines which take 100 per cent of their capacity wet gas to the absorption plant are dedicated fundamentally to the dry gas industry.

A Fundamentally and substantially.

Q But the separator and the tubing and all the rest in the well, which are responsible primarily for getting your wet gas into these gathering lines, are not dedicated fundamentally to the dry gas industry.

A They are not, sir.

Q You say they are not?

A They are not, no, because . . . . . .

Q Explain to me where you draw the line and how you draw it.

A You said, I believe, that the tubing, the well head and the separator equipment, is that dedicated exclusively to getting that wet gas and I say no they are not, because of the fact that the well head and the separator are utilized for the purpose of getting and producing oil and separating the oil from the gas. So it cannot be said that that equipment is exclusively used for wet gas.

Q I will leave it at that.

Would you say in those sections of the field where,

prior to this Inquiry being instituted and prior to certain Orders being made, there were gathering lines which took the wet gas to absorption plants and the residue product was flared, would you say that those lines were dedicated fundamentally to the wet gas industry?

A Yes, certainly, in that case.

Q So that whether or not they are dedicated to one or the other industry depends on whether or not you flare the gas, does it?

A It depends on the utilization of the wet gas in its final end product.

Q If you can sell your residue gas, it is dedicated to residue gas.

A Substantially, sir.

Q But if you cannot, it is dedicated to the wet gas industry?

A It is dedicated to the gasoline plant to which it is taken.

Q If Madison Company had in times past occasions when they could not sell all their residue dry gas and had to flare some, then did you have part of the pipe line dedicated to the wet gas industry and part to the dry gas?

A The Madison Company has not had that situation.

Q Well the Royalite.

A You said Madison.

Q Well then would you say at those times where part of the gas was flared downstream from the absorption plant, that part of the pipe line was dedicated to the wet gas industry and part to the dry gas?

A Oh yes.

Q Then I am right. It just depends on whether you flare it or not.

A I think so.

Q That is interesting. Now this might be a good point, Mr. Kirkpatrick, for us to discuss for a moment, the agreement between the Home Company and the Madison Natural Gas Company, Exhibit 84.

A Yes, sir.

Q I am going to suggest to you that from the information presently before this Board that there is no present need of any dry gas from the Home wells for purposes of supplying the market, is that right?

A Do you mind repeating that question?

Q I say there is no present need to obtain any residue dry gas from the Home wells covered by this Home contract, Exhibit 84.

A Well I do not know whether there is a present need or not but I assumed there was.

Q I am going to ask you to assume that for the next year we have sufficient gas capacity apart from these wells to supply the market and I note that this contract - you have read it by the way?

A I have read it, yes, in the past.

Q I note that it may be terminated by the Home Company at any time in the future. I think that is a fair statement.

A Under certain conditions, as I recall it.

Q Will you go this far with me that it is only at some, at present, undetermined point in the future that the privileges the Madison Company has here of getting residue gas may be called on, might be needed.

A Would you mind reading that question back please?

BY THE REPORTER (reading): Q. Would you go this far with me that it is only at some, at present, undetermined point in

in the future that the privileges the Madison Company has here of getting residue gas may be called on, might be needed.

Q MR. FENERTY: Assuming, I asked you to assume we had an adequate supply for, we will say, a year or two years.

A And we do not presently require this gas.

Q The right to get that gas only becomes of importance to Madison as a supply in the future, does it not?

A That is right.

Q And under this agreement you have no right to call for that gas in the future if the Home Company sees fit to take certain steps.

A That is right.

Q Will you tell me what possible object the Madison Company had in entering into a contract which does not guarantee them any supply of gas in the future. Do you know?

A No, I do not think I do.

Q I will suggest something to you and ask you if you know this. Do you know if it is a fact that the Royalite Company is interested in getting the natural gas content of the production called for by this agreement?

A That I do not know either.

Q You do not know that?

A No, sir.

Q But you do know that we have got a contract under which the Royalite will be ending up with some natural gas and Madison has no guarantee of anything that it is interested in, dry gas, don't you?

A Yes, that would appear to be so.

Q Do you think that justifies the Madison as a public utility, assuming the cost of this extension and seeking to charge

it back to the public until such time as the Home terminates the contract?

A I say that I think Madison is justified in passing the charges for a proportion of these facilities in proportion to the gas taken down through them. If the Home Company were to exercise its right at some date in the future and acquire ownership of a portion of the facilities, then, of course, the consumer would cease to have to pay any part of this total cost.

Q Let us get this again. We have agreed that Madison may never get a foot of dry gas that it needs to use.

A They might never get a foot?

Q That it needs to use.

A It is getting gas now.

(Go to page 2174)

Q I know, but it does not need it, it is just surplus now?

A It is not surplus if it is being utilized.

Q If you get gas now from the Home, you have some more repressuring cost, have you not?

A That is right.

Q You are adding to your expenses by getting Home gas now?

MR. CHAMBERS: Now is that a question or a statement.

MR. FENERTY: I have a habit of asking a question in the form of a statement. That is meant to be a question. "Is it not correct" I should say.

Q MR. FENERTY: You will assume I am not telling you something, I am asking you a question in every one of these things, is it not a fact that if you have your requirements for this year from other sources and you are getting dry gas from Home, you have increased your repressuring problem and the expenses of repressuring?

A It is true that if there is sufficient residue gas available...

Q Is that not a fact?

MR. CHAMBERS: Oh now, let him answer your question.

MR. FENERTY: Will you repeat the question so that Mr. Kirkpatrick will know what I asked.

MR. CHAMBERS: He is answering it.

MR. FENERTY: Then I would like him to answer that question, and if you still want to start out the way you did I will keep quiet.

(Reporter reading "Question")

Q "I am asking you a question in every one of these things. Is it not a fact that if you have your requirements for this year from other sources and you are getting dry gas from Home you have increased your repressuring problems and the

expenses of repressuring" ?

A You have increased the volume which is required to be repressured, yes. Whether you have increased the repressuring costs is questionable.

Q It may depend.....

A There are certain costs there anyway.

Q It might depend upon the point of whether you have reached where you have all you can handle?

A Yes, you have a greater volume.

Q But you might, as the result of getting gas from various sources, have increased costs?

A You may, yes, that is right.

And do you know of any reason for getting gas, from Madison's point of view, from Home and repressuring it now.

A I do not even know that Home gas is being repressured.

Q I see. Well do you know of any reason for getting gas from Home now, just leave it that way, this year?

A Well in the general interest of conservation I would think we would be interested in getting gas from any source so long as it is not going to result in flaring.

Q Yes, but if you are going to carry out a conservation scheme, is it not true that you shoul not have the provision for cancelling that agreement, should not that be a complete scheme throughout?

A I think we are overlooking one point in this, Mr. Fenerty, and that is that the facilities for the gathering, the installation and extension of the pipeline and the facilities for gathering,- to my mind it might as well be cancelled under direct Board orders rather than by way of agreement.

Q But subject to cancellation at the instance of Home at any time?

A Possibly so.

Q Oh?

A This contract has been consented to by the Board.

Q I am going to suggest to you and I am going to invite your opinion on this, I am going to suggest to you that a contract of the nature of Exhibit 84 involving the right of the Home Company to terminate and I suggest consequently giving no guarantee to you of any supply of gas at any time when you might need it, is a straight wet gas operation, first, last and all the time, what do you say about that?

A I do not see it that way.

Q You disagree with me?

A Yes. I cannot say that it is a straight wet gas operation.

Q I see. You suggest it is not. I suggest,- that does not meet with your approval, you think that is a dry gas operation?

A In the operation that dry gas, - the wet gas results in the ended product of dry gas.

Q You agree that you do not need it this year?

A No, I did not agree with you. You asked me to assume that.

Q You do not know about that?

A I do not know, that is an operating problem.

Q All right. Assuming you do not need it this year, assuming you have no right under the contract to call for it in the future, assuming those two things, will you tell me if you make those two assumptions, what justification from a dry gas operation is there for entering into the contract?

A Well assuming we do not need it.

Q Yes, now?

A And assuming they have the right to terminate it anytime in the future.

Q Yes.

A It would hardly seem likely we would have gone after that gas

Q It is hard to see any possible benefit to Madison, is it not?

A On the assumption that we do not need it.

Q But you do see, do you not, a distinct benefit to somebody who is interested in natural gasoline, through the wet gas?

A No Sir I do not.

Q Don't you?

A I see a fractional benefit to a gasoline plant of 20%, pardon me, not 20%, 80% of the content of that gas from day to day as it is used, less manufacturing costs.

Q And scrubbing?

A Yes.

Q Yes, that is a benefit, is it not?

A To any gasoline plant that extracts it.

Q Yes, so that we have here a contract put before the Board which discloses no benefits to the Madison and is a distinct benefit from day to day to somebody interested in wet gas extraction, is that not the final conclusion from everything you have told me?

A I have not agreed, Sir, that there is no benefit to Madison.

Q On the assumption?

A Well.....

Q Pardon me, on the assumption that you do not need the gas this year and that you cannot call for it in the future if Home does not want to give it to you, is that correct?

A I would have to consider all those assumptions.

Q I will leave it at that. I will leave it with you.

THE CHAIRMAN: Mr. Fenerty, to be fair to you and to the Witness, I should tell you that if Home and Madison had not entered into that agreement an order of the Board would have

compelled them to pick up that gas which was being blown in the air at the North end of the Turner Valley field.

MR. FENERTY: Yes, I understand that but I am dealing with this purely as to what I think is almost conclusive proof that this thing is not a dry gas industry but a wet gas industry.

THE CHAIRMAN: I am not questioning that. I am only explaining to you if there had not been that agreement there would have been a Board order.

MR. FENERTY: Exactly but I am endeavouring to show that that agreement would not even have got on the mimeograph machine if this had not been a wet gas industry, that is just what I am trying to show, it would not have got beyond the pencil draft. I may not be doing it but that is my purpose in cross-examination.

THE CHAIRMAN: I recognize your purpose all right.

MR. FENERTY: Well so much for that.

Q MR. FENERTY: Now Mr. Kirkpatrick, I want to turn to Volume 24, Page 1901, pages 1900 and 1901, you would not have that volume?

A No, I have not the volume here.

MR. CHAMBERS: I have it here.

MR. FENERTY: Would you please let the Witness have yours.

THE CHAIRMAN: That is dealing with Exhibit 74, Mr.Fenerty, is it.

MR. FENERTY: That was in connection with the statements which I was cross-examining about. It deals with remarks of yourself about statements which had been prepared

Q MR. FENERTY: If you will just glance through the remarks of the Chairman, the questions by the Chairman at the bottom of page 1900 and come over to 1901; it refers to statements prepared in connection with the various branches of the Royalite

Company's operations and you are asked at the top of page 1901:

"Q. But that is the purpose of preparing statements as far as can be done scientifically with relation to each Department.

A. That is correct.

Q So that the manager will know what is going on?

A Exactly."

Now I want you to note that question, "As far as can be done scientifically" for each Department and you say "That is correct" and then going on:

" Q. And such statements were prepared in respect to the Company's various operations?

A They were prpared with respect to the total operations and broken down for various purposes"

And then a little later on there is:

" The breakdown which I am talking about, there were special statements prepared with regard to the natural gas and the gasoline operations as a combined operation, and there were other statements prepared with respect to production as a whole" and so on, and then:

"Q. My point is that there are statements showing the results of the operations of each of the various divisions of Royalite?

A. That is correct.

Q And how often were these statements prepared?

A One annually, to my knowledge"

And going back to the question at the top of the page, these statements were prepared"as far as can be done scientifically. "That is the purpose of preparing statements as far as can be done scientifically with relation to

each Department". "Answer. That is correct".

Now that about sets out the situation, does it.

A It sets out what you have just read there.

Q I beg your pardon?

A It sets out what you have just read.

Q Well those are the facts are they not, as they are written down, are they, those statements were prepared "As far as can be done scientifically with relation to each Department"?

A Well I did not say it in just those words. The Chairman stated the purpose.

Q And you said "That is correct", these are the words of the Chairman of course?

A That is correct, yes.

Q And your answer is that the statement of the Chairman is correct, is that not what you say?

A Yes, that the purpose for preparing statements is to do them as scientifically with relation to each Department as can be done.

Q Yes that is it.

MR. CHAMBERS: Now I think in fairness you should refer to page 1908.

MR. FENERTY: Just a minute, page 1908.

MR. CHAMBERS: You are talking about the same thing there.

MR. FENERTY: What is it you want.

MR. CHAMBERS: They were talking about statements.

"One other thing. The Chairman asked you about the preparation of statements showing the division of the gas and gasoline business from the rest of your business and I believe that you answered him that the last statements were prepared first in 1939 or 1940.

A . No Sir, I said I believed my remark was intended to say that the statements with respect to a breakdown of the total operations had been made around 1939 or 40"

And he tells his reasons for that:

"They were prepared with respect to the income tax as it related to the Royalite Oil Company Limited to determine what of its operations produced what proportion of taxable income."

I just wanted to have it all before him.

MR. FENERTY: All right.

Q MR. FENERTY: But what I am getting at is this is done as scientifically as possible, that is the thing I am getting at?

A You re asking me if these statements were prepared as scientifically as possible, that is your question, Sir.

Q Yes, as far as can be done scientifically with relation to each Department?

A Yes.

Q With relation to each Department?

A With relation to each Department, absolutely.

Q And is a scientific method of making a breakdown any different as between departments and between a controlling company and a wholly owned subsiduary?

A The situation may differ. They were for different estimates of costs under these circumstances.

Q I will put it this way, would the most scientific way be the same in each case?

A Not necessarily, no.

Q No, what do you mean by "scientific", I am interested in that.

A The scientific preparation of a statement is a matter of

individual opinion to a very large extent.

Q You would not mean that the "scientific" way was the one that would give the best results under each circumstance, would you?

A Not necessarily, no.

Q Not necessarily but perhaps?

A Perhaps, yes.

Q Perhaps. I see. Do I understand then when you are preparing statements you are looking to what you can accomplish?

A Not at all, Sir.

Q What did you mean by that statement then that scientifically it might not necessarily but it might be a way which would give the best results for you under certain circumstances?

A It might depend upon the end object of the statement.

MR. FENERTY: All right.

(Go to page 2183)

Q Now our understanding is Mr. Kirkpatrick that you prepared these statements we have been talking about ?

A Are you referring to statements -

Q Referred to by the Chairman.

A No sir they were not prepared by me.

Q You did not prepare those ?

A Statements relative to the income tax matters were prepared by the Income Tax people of the Royalite Oil Company, not by me.

Q The statements we are now discussing and put before the Board today were prepared by you ?

A I beg your pardon. Oh yes, all these Madison statements.

Q My first question had to do with the earlier statements of 1939.

A Yes, statements relative to tax matters were not prepared by me.

Q But the latter ones now before the Board were the Madison statements ?

A Yes sir that is right.

Q Did you have anything to do with the preparation of statments in the way of instructions ?

A No sir.

Q To the persons preparing them ?

A No sir. My particular duties did not involve that particular branch of the accounting work.

Q But you have been at some stage familiar ?

A I have seen them but I have never had occasion to study them or examine them, no.

Q I think you have already told us with reference to at least one statement you prepared that costs in connection with gathering lines were allocated on the basis of gross returns ?

A I made that statement if I recall correctly in reference to statements which were prepared by the Royalite Company staff. For presentation to the Conservation Board.

Q That is an additional statement ?

A Yes that is a different set of statements I had reference to there.

Q Can you tell me whether that same basis appears on the statements we have been discussing. These ones discussed in 1939 or 1940 ?

A I have reason to believe they probably were but I cannot confirm that.

Q And have you reason to believe that any statements you ever heard of relates in connection with allocation of costs until the Madison Company appeared on the scene was on the basis of returns ?

A Have I reason to believe they were on the basis of returns ?

Q Yes.

A Yes, those statements I referred to as prepared for the Conservation Board were on the basis of returns.

Q And in using the Chairman's words, thought they were done as scientifically as far as can be done scientifically ?

A For the purpose for which they were prepared I believe I explained before.

Q Yes, I understand that.

A These statements were prepared for the purpose of determining the cost relative to the gas business and the gasoline business and it was a matter of indifference in what proportions those costs were spread.

Q It did not matter whether one Department showed a loss or not ?

A No sir. In fact it was the answer the Board was interested in.

Q The Royalite was not interested in whether they lost or made money in one Department ?

A Oh yes they were interested in making money.

Q But it did not make any difference for the purpose of the statement ?

A Not for the purpose of the statement, no.

Q So that the method of computing anything depends upon the purpose you have in mind ?

A On the circumstances, yes sir.

Q And what you are seeking to accomplish ?

A That is right.

Q And in most of the statements you were seeking to accomplish the best position you could accomplish in income tax matters.

A I presume so, yes.

Q And you have switched, I think that is a fair word, to volumetric computation of allocation of costs in connection with the pipe line from other methods previously employed. It is for the purpose of putting the Madison Company in the best position possible it can be in relation to this enquiry ?

A No sir.

Q Does that not follow as a matter of fact from what you have just told me ?

A I believe I have tried to explain to you that the statements in which I had a direct interest, namely the financial position arising out of the gas operations and gasoline operations, for I think it was the year 1943, was a matter of indifference in

just what proportions those gathering costs were determined, whether volumetric or gross realization, and to be frank with you we did not even consider the volumetric method at that time. It never crossed our minds as a possible approach to use.

Q You say it was a matter of indifference but I gather from your remarks the statement was of some scientific interest to do it right ?

A Yes it was of interest.

Q And that was the most scientific method you could think of then ?

A Yes it was the method we used whether it is subsequently the proper one -

Q And since this has become a public utility you have thought of another method ?

A I have thought of what I think is a proper approach to the problem. Not necessarily the only one, but I think it is a better approach.

Q Have you got the statement that we have been talking about available, the one for 1939 ?

A No sir, they are not in my possession.

Q They are Royalite statements ?

A Yes.

Q You have nothing to do with them or control over them ?

A No sir.

MR. FENERTY: I am wondering if the Board pleases whether or not the situation arising now as to a comparison of those statements. I am frankly anticipating at some stage that a Royalite Official will be on the stand who may have access to

and may have to produce the statements. That may or may not be so, but if that situation arises, I was wondering whether or not we should not have the opportunity of discussing comparative set-ups and figures with Mr. Kirkpatrick and if by any chance those statements are going to have to be produced by some one else, whether they should be made available while Mr. Kirkpatrick is in Alberta. I presume my friend does not see eye to eye with me.

MR. CHAMBERS: This matter you will recall came up in the early stages of the Hearing and I understood it was left. I opposed it then and I oppose it now, but it was left when you saw that a notice of motion should be made and the matter argued before the Board, and before any such Order is made I respectfully suggest that I should know what we are being asked for and I want to argue the matter before the Board. I take the position the Board has no jurisdiction. That is my submission. But I think you should give me notice of motion. In Volume 24 that matter has been there since last April.

MR. FENERTY: The only reason for asking it now, at the time these discussions arose there was no question of Mr. Kirkpatrick not being available if and when those documents were available. This has created a new situation. I can only make that suggestion. Well I suppose all I can do is make the suggestion. I cannot compel anyone to do anything.

THE CHAIRMAN: I have no power to compel this witness to produce them. The only suggestion we might make is if you consider that the statements which were prepared for an entirely different purpose nevertheless might have a bearing on this particular issue and if a Royalite Official will be in the box

at a later date, Mr. Chambers might consider whether or not the production of those documents at that later date might become inevitable or whether he might consider the possibility or propriety of producing them now. In other words, bow today to the inevitable some months from now.

MR. FENERTY: I thought my suggestion might be of use to Mr. Chambers.

MR. CHAMBERS: You have been very complimentary to all my witnesses and I appreciate it very much, but aside from anything else I have considerable reason to doubt whether these statements have any relevancy at all. Admitting they were prepared for something else, if we are going into that statement I can think of a lot more statements I would like to know about, for instance a prior gas company statement and I would like to be treated the same -

MR. FENERTY: Well that is all I can do at the moment.

Q I am going to ask you as to any recollections you may have. You did answer as to recollections of another statement. Am I correct in my understanding that the Royalite had its operations divided into a number of divisions, perhaps oil, gas, wet gas and so on ?

A I think I explained that last April or May if I recall correctly. In this way, the Royalite Company had never maintained in its accounts a separate division of records exclusively relating to any one Department. Its full operations were treated on a corporate basis and the statements we have been referring to just recently, the tax statements, the conservation board statements were prepared essentially from those corporate records.

Q It is true however to say that as far as you know none of the allocations as between one Department arrived at by computation similar to those appearing in Exhibit 78, M-9-A-44 where external charges are computed. I am referring to external charges of $30,000.00.

A Yes, I think your question is, does our procedure here differ from the method in which Royalite apportioned its general charges for any particular statement it may have made.

Q Yes I am really repeating myself. You have covered that.

A These statements are prepared on the basis of attempting to assign every dollar.

Q To see if I understand this. I would like to go over it again. Let us take Exhibit 78. We have those external charges, $30,631.54. Do I understand those external charges are the charges to Royalite and perhaps the Valley Pipe Line ?

A Yes sir.

Q That is what they consist of ?

A Yes sir.

Q And those figures, $30,631.54 represent the 5 percent Mr. Blanchard was discussing with you this morning ?

A That is right.

Q A difference between 25 percent of the returns from wet gas operations and 20 percent produced. That is one system. Then I understand in your report Exhibit 79, where you have a total on Exhibit M-9-A-44, you have a total of $56,084.08 for external charges for compression and -

A Gathering.

Q And that was made up on the volumetric system ?

A That is right.

Q Now on the basis of the amount in volume of content extracted from wet gas during the wet gas operations ?

A That is right plus the proportion amount of plant fuel.

Q Yes, the principle one is the gas ?

A Yes, that is right.

Q It has nothing to do with the volume of gas treated or going through the absorption plant ?

A It has a direct relationship. The percentage arrived at is based on the volume which goes through the plant. The volume which comes into the plant is opposed to the volume that goes out of the plant substantially represents the percentage which makes up the $58,000.00.

Q That is right, but it is on the basis that the absorption plant is interested in perhaps 13 percent, ten to twelve, to thirteen percent of the wet gas ?

A Well it happens to be at 9.45. That figure may very well vary.

Q It is on the theory that the absorption plant is interested in 9.45 of the wet gas not 100 percent of it ?

A That is right.

Q That is two systems ?

A May I just explain a point there to remove any confusion. The $58,000.00 as I explained to Mr. Blanchard this morning was a computation prepared on an estimated basis and had we reached the point where this Board had given us their blessing on that particular volume that would have been the amount charged Royalite on that plant. Now we are asked to prepare the actual for 1944 and that I say is the difference that can be adjusted.

Q But it is a different base for instance if you had the basis for computation that you had when this was prepared applied to the actual figures it would not come out $30,000.00 ?

A I thought I had made it clear before that the 5 percent has no relation to anything. It was the figure tentatively taken to arrive at some interim charge to the plant.

( Go to Page 2192 )

Q I think you did say that at the beginning, but did you not in answer to my learned friend, Mr. Blanchard, say that that represented the difference between 25% and 20%?

A Yes, that is what it amounted to.

Q That is what it is, is it not?

A The 5%.

Q Those figures here of 25% and 20% were actually discussed in all seriousness?

A That is right.

Q And that is the 5% we are talking about?

A It makes the $30,000.00.

Q It is the 5%, that is the difference between the 25%, the value of the contents of this wet gas that Madison gets and the 20% that it pays out?

A That is right.

Q And not another 5%?

A Yes, not another 5%.

Q So that there is nothing haphazard about it?

A I beg your pardon?

Q So that there is nothing haphazard about it? I just want to get it clear?

A That is the 5%.

Q Now, already we have two systems, that we have been discussing here and one of them is the volumetric, that is right?

A That is right.

Q Now I am going to suggest to you that this company at some stage of these proceedings was a more or less enthusiastic advocate of a third system, do you remember that? And that is based on gross returns or values?

A We were neither an advocate of one system or another. We were attempting to arrive at some procedure for distributing the

cost for performing those services.

Q I am wrong there. I should have said Royalite had been an advocate of the third system. I want to refer you to Mr. Latham's evidence. It is contained in Volume 4, page 208, Exhibit 15. I wonder if we have that here by any chance? I think it refers to that. I am reading now from page 208:

MR. CHAMBERS: What page?

MR. FENERTY: 208. Mr. Latham was on the stand and being examined by Mr. Chambers. At the top of the page;

" MR. CHAmbers: Would you please give to the Board the contents of that memorandum and any comment you care to make as you go along.

A This is a memorandum setting forth the proposed basis for dividing costs of operating the No. 1 and the No. 3 Compressor Plants and the Gas Gathering lines between Madison Natural Gas Company Limited and Royalite Oil Company Limited."

And here are quotations which apparently are from that report. I do not think I need to read that. And you see there a statement from the Report indicating that Royalite Company recognized that it is equitable that it should bear a part of the costs of operating the two Compressor Plants and the Gas Gathering line. And then there follows a statement of the various factors, the direct operating expenses and so on. And then the following statement:

" It is also suggested that the total costs as estimated from the above mentioned factors be apportioned in ratio to the respective revenues from gas sales and natural gasoline sales."

You see that at the top of page 209. And then I want you

jump over to the top of page 310, the third line:

" As to the proposal that the costs be divided in proportion to respective revenues, this method is one of the generally accepted methods of allocation, and apparently there is no method more equitable."

Do you see that?

A Yes sir.

Q I take it you are in total disagreement with that?

A Yes,sir, obviously.

Q And it is a third method?

A Yes.

Q And ineach method that has been advocated either by Royalite or Madison as they progressed the results have been a lessening thecharge in each case to the Royalite Company for the same service?

A Let me say this.....

Q Is that correct, first?

A Yes, that is correct. But I would like to qualify that by saying that the method that you spoke of which resulted in the $30,000.00 is apparently a simple and tentative arrangement. We could just as easily have said "Give us $30,000.00 until the Board decides how it is to be set up." It is not a method or any arrangement.

Q Mr. Kirkpatrick, I will ask you a question which has been used quite frequently here, are you by any chance frolicking with another method?

A No sir.

Q You have got a last one?

A This is mine.

Q Now in connection with that apportionment on the basis of return, gross return, was there taken into consideration the value of the 20% that the well owner got the benefit of?

A In the statements with which I was concerned it was 100% of the moneys received for the gasoline which automatically included the 20% which eventually went to the producer, and 80% to the plant.

Q You will have to excuse me because I am not at home in accounting, but I am trying to get at this. When you say that the distribution was approximately on the basis of 40% to the natural gasoline end of it and 60% to the dry gas end, did that 40% represents the Royalite's 80% or 100%?

A 100% as I recall it, I am sure.

Q And on the other side you would have the 2 cents paid for the gas?

A No 7¾ received.

Q That includes the 2 cents?

A Yes.

Q So that it is on the basis of 100% of the whole thing?

A Yes, 100% of every dollar.

Q Now I was interested in something that occurred this morning earlier, when you mentioned the allocation of compression costs downstream from the absorption plant, that is the allocation as between a market and the repressuring, as I understand it, in that case you adopted the system of charges being basedon the horsepower employed, because of the fact that the other factors being considered were not equal, that is the pressure in the pipes and the pressure in the gas cap, that is right is it not?

A We suggested the horsepower basis because we think it provided the measure of power.

Q And I am right that you depart from the volumetric method

there because the other things considered were not equal.

A That is right.

Q And I suggest to you it is equally sound to depart from the volumetric method when you are measuring the apportionment of the cost of transmitting wet gas where the other elements for consideration are not equal, would not that be so?

A That is possibly so. I would not disagree with you.

Q And the elements for consideration, namely, the value of the gasoline again and what you get for dry gas in no sense correspond, do they?

A I do not think so, no.

Q Therefore it follows that the other elements not being equal, the volumetric method is unsound, is it not?

A I do not think so, but.....

Q If you come to that conclusion?

MR. CHAMBERS: Are we speaking of the volumetric method with regard to the gas when it is wet?

Q MR. FENERTY: Mr. Kirkpatrick, I am suggesting to you that you just came to that conclusion in your series of answers to my questions in the last three minutes.

MR. CHAMBERS: And he disagreed with you.

MR. FENERTY: I think I am entitled to ask him.

MR. CHAMBERS: You did not give him an opportunity to finish his answer.

THE CHAIRMAN: Gentlemen, I do not want bickering in this room.

MR. CHAMBERS: I want to object.

THE CHAIRMAN: What Mr. Fenerty has said is a quite proper deduction. If he had just let it go at that, from those answers we could deduce what is meant.

MR. CHAMBERS: My learned friend interrupts the witnesses. He does it with a good intention but he is prone sometimes to cut the witnesses off.

MR. FENERTY: When we are getting to the stage where my learned friend is paying me a compliment it is a dangerous point from his point of view, when he bobs up to interrupt me, and it is hard for my logic to be interrupted.

MR. CHAMBERS: I do not try to be technical, but I think in fairness to the witness he should be allowed to answer.

MR. FENERTY: Now if there is anything that you want to be read to you to answer that question, that will be all right. Would you please answer that question, I would like you to answer it.

THE CHAIRMAN: I think it follows as a necessary deduction.

MR. FENERTY: I am willing to leave it at that.

THE CHAIRMAN: That that method might be unsound, but then the other two might be worse than the third.

MR. FENERTY: All in effect I did was to make a statement to the witness whether two and two added to four.

MR. CHAMBERS: I think the question should be read and I think he should be allowed to answer it.

THE CHAIRMAN: I think because of the course of the questions and answers, Mr. Kirkpatrick was driven to the conclusion that the volumetric method was as bad as the other method, and Mr. Kirkpatrick disagrees.

MR. CHAMBERS: I just want him to answer it, the question. He was going to add something to it. I just want him to answer it if he has an explanation.

MR. FENERTY: Perhaps it would be more effective if he explains it to my learned friend on re-examination,

because, to be quite frank, he cannot explain it to me on cross-examination.

Q Now, Mr. Kirkpatrick, I will not be very much longer. I want to come to Exhibit 78 again, Exhibit M-9-A-44, and I want to draw your attention to two items here. I will not be very much longer.

THE CHAIRMAN: Take your time, Mr. Fenerty,

Q MR. FENERTY: Turning to the Boiler Plant and Electric Plant. As a matter of fact, for the record, so that I will know if I understand it, and I think it is elementary, but you will pardon me for asking. As I understand it, your gross operating costs are $81,860.51, and that includes all the preceding items. We will take the Boiler Plant. One is sufficient. Now you have explained the administrative and general expenses, which you feel are fairly allocated to the Boiler Plant operation, and the proportion of depreciation which is properly allocated in there, the return on capital employed, and those are the totals which make up your gross operating costs?

A That is correct.

Q Yes. And that necessarily includes a proportion, a rate of return which you expect may be allowed on those operations?

A Not which we expect, sir. We are looking at the actual statements here.

Q At the actual?

A Yes.

Q And the actual is 7½% approximately?

A 7.046 net.

Q Yes. And we come to this column "Less External Charges" $58,289.14. And my understanding is that represents the proportion of the whole which you have charged against Royalite

and the Valley Pipe Line Company?

A Yes sir.

Q In connection with services supplied them?

A Yes sir.

Q And that includes, does it not, a rate of return of 7 something, something over 7%?

A Now I would like to check this, but I believe that calculation of fifty-eight thousand was based upon 9½% net return.

Q Yes. Was based on that?

A That is correct, in my understanding.

(Go to Page 2200).

Q Yes. Now your Company is a commercial undertaking. It is there for the purpose of making a profit, is it not?

A That is right.

Q And the matter of a profit from the sale of power and the sale of steam by you to the Royalite Company has not heretofore been regulated by this Board and as far as you know is not the subject matter of regulation now is it?

A I cannot tell you whether it is the subject matter of regulation or not. It is part of the Madison Company's operations and I suppose this Board will be interested in what is going on.

Q Now Madison Company acquired gathering lines without which the Royalite Company could not operate its gasoline plant.

A Wihtout which it could not get gasoline.

Q Without which it could not get gasoline, yes. Would you say that 7 per cent or even 9 per cent would be a reasonable rate to charge any other institution that wanted services from you . . . . .

A You are going into the realm of economics, Mr. Fenerty and I am not an expert at that. I have no opinion of what would be fair. I know what I would like to see.

Q I thought you might be. At all events, you have made up your charges to the Royalite Company and the Valley Pipeline Company on the basis of a return of 7 per cent.

A I explained a moment ago on the basis of 9½ per cent.

Q The statements show 7 per cent actual.

A No. Just refer to that submission again please.

THE CHAIRMAN: The end result shows 7 on the overall operation.

A But the charge to the Valley Pipeline Company or the Royalite Company for each thousand pounds of steam or each kilowatt

hour of energy which they received in 1944 was based upon the estimated cost of manufacturing those services, using 9½ per cent net as the basis for the calculation. So that the $58,000.00 is on the 9½% basis and resulted in a deficiency of some $3500.00.

Q Do you suggest that is a reasonable rate of return where the guarantees that go with public utility operation are not present?

A I have no opinion, sir, as to whether it is a reasonable rate of return.

Q A reasonable rate?

A It certainly is a reasonable rate, I think.

Q Let us get this. You have got the complete control of the gathering lines.

A That is right.

Q That Royalite needs to carry on its gasoline operations. You have got complete control of the steam power that Royalite needs, about three-quarters of it they need do they not?

A That is correct.

Q I suggest to you that a normal, commercial operation where there are any inherent risks not protected by public utility practice would justify a very heavy charge for that kind of service. Have you any comments to make on that suggestion?

A No, sir, I have not. I am not a student of rates of return.

Q I suggest to you that you personally, from what you do know, would laugh at the idea of someone else in the Valley getting these services at a rate which would give 9½ per cent.

MR. CHAMBERS: I would suggest that the witness does not have to answer that question if he does not want to.

THE CHAIRMAN: I think this witness can look after

himself very well indeed. As you remarked yourself on another occasion, he does not need the benefit of counsel.

MR. FENERTY: I am beginning to think I need protection and not the witness.

Q You have nothing to say about that?

A No, I have not. Would you repeat that question please, Mr. Taylor?

BY THE REPORTER (reading) Q. I suggest to you that you personally, from what you do know, would laugh at the idea of someone else in the Valley getting these services at a rate which would give you 9½ per cent.

A I would be very happy to get a rate of 9½ per cent for services of this kind provided I could see there was a continuity of the life of my undertaking and enterprise.

Q You suggest that a rate of 9½ per cent is quite adequate for an ordinary commercial transaction with no protection such as is afforded by utility practice, would you?

A I would say it was a nice rate of return to get.

Q Is that so. Now you are going to come along with me. You would suggest as an ordinary commercial transaction, with no protection in the way of amortization or anything else, that 9½ per cent is a fair rate of return is it?

A I would be prepared to put money into an undertaking which would return me 9½ per cent, if I had a reasonable guarantee that I would have a service which would be in operation long enough to give me my total capital return without public utility regulation or guarantee.

Q I suggest to you if that is true it follows that without the safeguards that are given in the way of return of capital under utility practice and order that a rate of something

less than the open rate you talk of should necessarily be a fair rate. What do you think about that?

A You are suggesting, I believe, that this same operation under public utility regulation, with a fair guarantee of the return of the money invested in it, that 9½ per cent should be something less than the amount we spoke of in the same undertaking but unregulated enterprise. You are speaking first of all about a boiler plant which I would be prepared to put money into but here we are not looking into a boiler plant business but a gas business which has all the inherent risks of a gas business. The boiler plant happens to be a part of this operation.

Q This Madison Company, we will just take the boiler plant, the Madison Company has acquired a boiler plant which I understand is greatly in excess of its own needs, is that right?

A That is apparent from these statements of costs.

Q And with the steam from that plant being used and intended to be used to the extent of perhaps three quarters, although I do not know the exact fraction, by the Royalite Company, that is right is it not?

A And the Pipeline Company.

Q And it is making a submission here that it should be out of the rates that are arrived at, able to fully amortize all these costs of that plant which is in excess of its needs is it not?

A That is right.

Q And it justifies that on the ground of making a service charge to the Royalite Company?

A That is right.

Q I am going to ask you again, if you do not think under those

circumstances, with the Madison Company coming to this Board to have full protection for all its costs of that boiler plant that it should not make a charge against the Royalite Company greatly in excess of the one which would provide a return of 9½ per cent as a matter of ordinary sound business.

A I do not think they should make a charge to the Royalite Oil Company or the Valley Pipeline Company in excess of any rate of return beyond that which is applied to the entire undertaking.

Q Your answer is, I take it, you think everything about this, regardless of whatever you are seeking to accomplish, is based on the soundest and most scientific practice from any point of view, is that the result?

A These statements are my answer. Taking the plant and equipment which we acquired and the 9½ per cent rate this is the answer that comes out.

Q I have one more question on that. You have told me about the scientific method for the purposes sought to be accomplished. I am going to ask you whether if your interest at the moment was not just your utility division and you were left to make a statement up for income tax purposes or perhaps for interdepartmental purposes as before, you would now revert to the previous practice.

A No sir. I have given sufficient thought to this volumetric method of approach that I would stay with that.

Q Under all circumstances?

A Yes, I think so.

Q You think the most scientific method is the one which should be applied under all circumstances?

A Sir, would you repeat that?

Q You think the most scientific method is the one you should

apply under all circumstances?

A If there is any science to the method.

Q Do you remember now you have just told me the result of your experience and you would apply this method?

A I would now.

Q In every situation?

A Every similar situation, yes. An operation which involves the rendering of Gas Company service to consumers along the route I say the relative costs are determined in proportion to the volume used.

Q The word "similar" did not appear until we got into the third question in sequence, did it?

A No, because that is my own word "similar".

Q I am suggesting prior to this you told me as a result of your experience if you were preparing statements for the purposes you had previously, you would now adopt this method.

A I would, yes sir.

Q I say it follows from that that whatever purpose it is the most scientific method would be the one you would adopt.

A For the purposes for which the statements were prepared it made no difference relative to compensation matters but for those purposes I would now apply the same procedure, the volumetric approach.

Q For any purpose would you apply another system?

A I have had no occasion to apply it to any other purpose.

Q Just one more question, would it be possible without too much trouble if you would let us have a statement of the sixteen thousand . . . . . In Exhibit 78 we have provision for taxes on property Exhibit 76 of $163,169.00.

A On the last page, is that the figure you are referring to, Mr. Fenerty?

Q That is on the last page of Exhibit 78?

A Yes.

Q You gave on the stand an explanation and I was wondering if it would be possible to let us have that in the form of a statement.

MR. CHAMBERS: I am not clear on what you are wanting. I am not clear whether Mr. Kirkpatrick is.

A I think Mr. Fenerty is asking for a break-down of that provision for taxes.

Q MR. FENERTY: In other words a computation reaching that result.

A $163,169.00?

Q Yes.

A Yes.

MR. CHAMBERS: Yes we will do that.

MR. FENERTY: Thank you.

.....

CROSS-EXAMINATION OF THE SAME WITNESS BY MR. STEER.

Q Is this volumetric method you have spoken of a technical term?

A I think Mr. Hill said it was a semi-technical term, sir.

Q I have a recollection of asking someone, probably it was Mr. Hill, about this point. As I understand the application of the method in this case it consists in computing what percentage of the gas that goes into the absorption plant is actually used in that plant?

A Yes, that is right.

Q We will assume for the moment that that is 20 per cent and according to the method, although the operation could not be carried on in the absorption plant at all without

100 per cent of the gas, that is true?

A No. The absorption plant would not be able to extract this 20 per cent of content without 100 per cent of the gas.

Q It must handle the whole of the gas that comes through these gathering lines.

A That is correct.

Q And according to this method of division of costs it is said that the only part of that gas it really needs is 20 per cent, on our supposition.

A No the only part that it extracts and retains in its possession is 20 per cent.

Q I wonder perhaps if you would give us an estimate of the amount of shrinkage that takes place in the absorption plant?

A It is something around the order of 7 or 8 per cent according to the calculation I have before me here.

Q So that of 100 per cent of the gas that goes into the absorption plant the Madison Company treats in its scrubber about 92 per cent approximately.

A Something in that vicinity, yes.

Q Now is not this a reasonable proposition that the absorption plant requires for its purposes 100 per cent of the volume and it cannot get along without it. That is right, is it not?

A I think it is, Mr. Steer. It requires 100 per cent of the volume to obtain the present production of natural gasoline.

Q And the scrubbing plant uses 92 per cent of the volume?

A Yes, sir.

Q I wonder why that proportion of operating costs in each case should not be 100 over 192 in the one case and 92 over 192 in the other. Do you follow me? I am suggesting to you

that is the proper way to apply the volumetric method.

A I think I see what you mean there, Mr. Steer. I have not considered that approach to it.

Q I am not going to take very much time in view of the cross-examinations that have preceded me but I would like to clear up a point or two in my own mind. My learned friend, Mr. Fenerty, referred you to one of your statements in which you said that at some time there had been a division made between the absorption plant operations and the scrubbing plant operations in the proportion of 40 to 60.

A I think Mr. Fenerty asked me the question as to what the approximate proportions were in terms of gross revenue and I think I answered that.

(Go to page 2209)

Q. Yes, that is right and you answered "40%" and at sometime or other in the history of these operations that was regarded roughly as the proper division of costs?

A For the purposes of the statements which were being prepared, Mr. Steer, that is correct.

Q Yes, and am I right in this that if we were looking at M-12-D-1944, that figure of 510 thousand dollars which we see there would represent the total cost of the operations for the year 1944, is that right?

A Total estimated costs, yes.

Q Yes, and if we apply the 40 - 60, if we were to apply 40, 60 to 40, the 60 to 40 which we were just speaking about, Royalite ought to bear 40% of that 510 thousand dollars, is that right?

A I will just check that for a moment, please. On the assumption that that method was used I think that is a correct statement,

Q We will assume for the moment, Mr. Kirkpatrick, that the Royalite Oil Company is asked to prepare a statement showing the costs, its costs of producing natural gas, are you the person in the Royalite employ who does that?

A No Sir.

Q Who would?

A I do not know whom they would assign that particular work to, possibly Mr. Latham, an employee of the Royalite Company.

Q While you were in Royalite's employ , were you the person who would do it or are you still in the Royalite's employ

A No Sir, I am not. I am a Madison employee so far.

Q But prior to the incorporation of Madison you were employed by the Royalite?

A I would very likely have some association with such a problem.

Q Yes, and if it ever transpired that this Board would want an examination of the Royalite's books for the purposes of ascertaining the costs of the production of gas, you are perhaps more familar with those books than any other former, any other present employee of Royalite, would that be right?

A I would not say I was more familar with them at the present time because I have not been associated directly with them for a year and a half. The bulk of my time has been spent with Madison.

Q In your evidence with respect to M-10, I mean the reading of that report, I noticed that you talk about your pipes being buried from five to five and a half feet under ground and that is one of the reasons that there is no salvage to those pipes.

A One of the reasons which mitigate against that salvage, yes.

Q If the pipes were closer to the surface there would be a greater salvage value to the pipes?

A The only value which would be greater would be the cost of, because the cost of removing them would be less.

Q Have you any idea why these pipes have to be buried five to five and a half feet under ground?

A Well I would assume because of the low temperatures which are encountered when the winter season is here in Turner Valley.

Q Would that be below the frost line?

A I would not know. I do not know but I guess it would be, Sir.

Q I suppose Stevens-Guille would be the man to talk about that?

A I would think that five and a half feet would be below the frost line but I would like to check it.

Q I notice a tendancy to assume that the consumers of gas were going to bear the expenses of this undertaking, - that is not your evidence?

A What understaking do you refer to.

Q The Madison undertaking?

A The entire undertaking.

Q The entire undertaking.

A I have not taken any such assumption in my statements and my statements are intended to show what it costs to do the job.

Q And you do not care who bears the cost.

A Well I hope that Madison does not bear it, that they are in a position to recover the cost.

Q You would agree I think that there are certain aspects of this s ome which are of particular benefit to the producers of crude oil?

A In what sense, Sir; I can see a benefit in the sense that there may be gas from these crude oil wells which is now entering the market for the first time.

Q Yes?

A That I would say would be a benefit.

Q Yes, and I would suggest to you that the producer of crude oil whose surplus gas is repressured he will ultimately, he either now or sometime in the future will be paid and he will get a substanti l benefit.

A He gets a benefit to the extent that that gas would not have been a money making proposition had it been flared.

Q Yes, and then it is obvious I think that the Royalite and B.A. Absorption Plants in any event obtain some substantial benefit?

A From this crude oil gas which otherwise would have been flared.

Q Yes?

A I cam see that the operations for the purposes of extracting gasoline will be prolonged by reason of that gas now being made available.

Q Yes, and you will admit that a substantial benefit, I mean you will admit that is a substantial benefit?

A Well it depends on how long it is prolonged but I would say looking at it from a general view point there is a prolongation of the operating life of those plants and a greater opportunity to recover from it.

MR. STEER: That is all, thank you.

(Go to page 2213)

THE CHAIRMAN: Mr. McDonald.

CROSS-EXAMINED BY MR. McDONALD:

Q Just one thing, Mr. Kirkpatrick, in M-9-44 - -

A Is that the actual you are referring to, Mr. McDonald ?

Q Yes.

A Exhibit 78.

Q Exhibit 79.

MR. CHAMBERS: It is Exhibit 79 you are referring to Mr. McDonald.

MR. McDONALD: Yes.

Q MR. McDONALD: You have a contingency for unforeseen expenses of $20,000.00 ?

A Yes.

Q Then Exhibit, it is M-7, I have not the Exhibit number marked on it.

THE CHAIRMAN: Exhibit 74.

Q MR. McDONALD: Exhibit 74 and Schedule M-7-C ?

A Yes.

Q You have, that is a statement of estimated cash working capital ?

A Correct.

Q At the bottom of the page, "Cash working capital for contingency funds $43,554.90" ?

A Yes.

Q Now it would appear that, and I am referring here to the estimate in the first part of M-7, or Exhibit 74, that the charges for the working capital allowance and the contingency in your calculation in your M-7-44 are the same ?

A Oh no sir, the two are entirely different things. Perhaps I can

best explain that to you by stating it would have been just as easy for us to have said, in preparing M-9-A "We feel that we have not provided for unforeseen expenses which may arise during the course of operations during the year and let us increase that by 5 percent.", that is the approximate relationship but we chose not to do that. We put the $20,000.00 in there in the expectation that we may have been leaning backward in determining those operating costs, and that fact seems to have been borne out by comparing the M-9-A estimate with the actual for the year. We were too low. Our $354,000.00 should have been $372,000.00 approximately. They are two different items, Mr. McDonald.

Q Well on your over-all operation then you really have for contingent direct expenses, prepaid expenses and construction - -

A Now we are speaking of the working fund ?

Q Yes, the working fund which comes to a total of $63,554.90 - -

A No sir, that is not right. This $43,000.00 is altogether different from the $20,000.00. The $20,000.00 is just, we say that we are probably too low in estimating operating expenses and we were too low and that was set forth in our 1944 actual figures. The $43,554.90 is a part of the working cash capital. It has no relationship to the operating expenses.

Q Well prepaid expenses such as fire insurance, that would be a direct operating expense, would it not ?

A Only in the proportion of the three year premium which applies to this year.

Q Now would you say a construction, an ordinary construction of some new undertaking during the year, would that be a direct expense ?

A You have reference to capital inprovements, Mr. McDonald ?

Q Yes.

A No sir, that is not a direct expense.

Q Now in regard to administration and general expense, there is some division of the services of some officers between Madison and other Companies ?

A That is correct.

Q Now how many officers are involved ?

A Two, Mr. Trammell and myself.

Q And how do you apportion that ?

A On the basis of individual time spent.

Q And that time would vary from year to year ?

A We anticipate it will come down and we have I think attempted to show that trend in our future administration costs.

Q For instance this year you might give 90 percent of your time to Madison and the next year less ?

A It would all depend, at the beginning of the operations a great deal of time was given to setting the thing up and during the course of years, it was naturally, approximately one hundred percent of the time, but once the undertakings are operating in a normal way we do not anticipate the burden on administration with respect to these salaries will continue as it is.

Q Now dealing with the absorption plant, Mr. Kirkpatrick, as I understand it in order to deliver dry gas to the market you must have the gas treated in an absorption plant ?

A You are referring to the fact that the deleterious substances must be extracted ?

Q Yes.

A Yes, that is my understanding. It is not a safe marketable

product without that operation.

Q So if there was no Royalite absorption plant in operation, some other plant would have to do that ?

A I would assume so.

MR. McDONALD: That is all, thanks.

THE CHAIRMAN: We will adjourn now until tomorrow morning.

MR. CHAMBERS: If the Board pleases, it looks as though we may finish with Mr. Kirkpatrick early tomorrow and I [illegible] prepared to put Mr. Stevens-Guille in and deal with the sharing position if that is agreeable to the Board and the others present. I think with the time at our disposal that we would be sure to finish with him on that subject.

THE CHAIRMAN: I think that would be proper.

MR. HARVIE: Would it not be more convenient to finish the cross-examination ?

MR. CHAMBERS: If we did then we might not finish the sharing position and I want to finish the sharing position if we start with it.

THE CHAIRMAN: And then finish the cross-examination next week if we have time.

MR. FENERTY: We had the idea when Counsel were discussing that matter before the long adjournment, we had arranged the order of continuing the cross-examination and it was arranged that I might go on with some further questions, which questions may take a little while.

MR. CHAMBERS: If you intend to go on with your cross-examinations of Mr. Stevens-Guille first, I doubt whether we should start the sharing position.

MR. FENERTY: I mean if we go on with my cross-examination for instance it may take a little while.

You are suggesting that we go on with the sharing position first and then have our cross-examinations afterwards.

MR. CHAMBERS: Yes.

THE CHAIRMAN: Yes, and then go on with the cross-examinations if the sharing position is finished in time.

MR. FENERTY: That is satisfactory.

(The Enquiry here adjourned to be resumed at 9.30 A.M. June 21st)